



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Release Number: **201149031**
Release Date: 12/9/2011
Date: September 13, 2011
UIL Code: 501.33-08
501.03-30
501.33-00
501.36-01
504.50-00

Contact Person:
Identification Number:
Contact Number:
Employer Identification Number:
Form Required To Be Filed:
Tax Years:

Dear

This is our final determination that you do not qualify for exemption from federal income tax as an organization described in Internal Revenue Code section 501(c)(3). Recently, we sent you a letter in response to your application that proposed an adverse determination. The letter explained the facts, law and rationale, and gave you 30 days to file a protest. Since we did not receive a protest within the requisite 30 days, the proposed adverse determination is now final.

Since you do not qualify for exemption as an organization described in Code section 501(c)(3), donors may not deduct contributions to you under Code section 170. You must file Federal income tax returns on the form and for the years listed above within 30 days of this letter, unless you request an extension of time to file.

We will make this letter and our proposed adverse determination letter available for public inspection under Code section 6110, after deleting certain identifying information. Please read the enclosed Notice 437, *Notice of Intention to Disclose*, and review the two attached letters that show our proposed deletions. If you disagree with our proposed deletions, you should follow the instructions in Notice 437. If you agree with our deletions, you do not need to take any further action.

In accordance with Code section 6104(c), we will notify the appropriate State officials of our determination by sending them a copy of this final letter and the proposed adverse letter. You should contact your State officials if you have any questions about how this determination may affect your State responsibilities and requirements.

Letter 4038 (CG) (11-2005)
Catalog Number 47632S

If you have any questions about this letter, please contact the person whose name and telephone number are shown in the heading of this letter. If you have any questions about your Federal income tax status and responsibilities, please contact IRS Customer Service at 1-800-829-1040 or the IRS Customer Service number for businesses, 1-800-829-4933. The IRS Customer Service number for people with hearing impairments is 1-800-829-4059.

Sincerely,

Lois Lerner
Director, Exempt Organizations

Enclosure
Notice 437
Redacted Proposed Adverse Determination Letter
Redacted Final Adverse Determination Letter



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

Date: July 22, 2011

Contact Person:

Identification Number:

Contact Number:

FAX Number:

Employer Identification Number:

UIL #;s

501.03-08
501.03-30
501.33-00
501.36-01
504.50-00

Legend:

<u>D</u>	=	date
<u>M</u>	=	web site
<u>N</u>	=	computer software
<u>S</u>	=	state
<u>T</u>	=	city
<u>U</u>	=	dollar amount

Dear

We have considered your application for recognition of exemption from federal income tax under section 501(a) of the Internal Revenue Code ("Code"). Based on the information provided, we have concluded that you do not qualify for exemption under section 501(c)(3) of the Code. The basis for our conclusion is set forth below.

Issue

Do you qualify for exemption under section 501(c)(3) of the Code? No, for the reasons stated below.

Facts

You were incorporated under S law on D. Your Articles of Incorporation ("Articles") state your purpose is to provide help to families struggling to make ends meet by putting together a solid financial plan with an emphasis on budgeting and saving and to help families in crisis with monetary support from time to time. Your Articles also state you are organized exclusively for 501(c)(3) purposes.

Your bylaws state your purpose is to assist lower and middle-income families and individuals with the development of household financial, budgeting and savings plans.

Your activities consist of providing comprehensive, one-on-one financial planning and counseling to middle and low-middle income households, who are not deep in debt, do not have a household budget and who have not saved enough for retirement or other important financial goals. You estimate this category covers about two-thirds of the population in T and your typical client would be age , with household income of at least \$, inadequate savings for college and retirement, but less than \$ debt. You do not intend to serve those who are deep in credit card debt. You plan to advertise weekly in local newspapers with distribution to about 60,000 households. You expect that you will serve between 100 to 200 clients per year.

Your financial planning and counseling has two parts: presentation and planning. The presentation on financial planning is a two hour long, 52 page PowerPoint presentation on introduction to financial planning, which emphasizes the importance and need for financial planning. It covers the need for financial planning, successful family planning, understanding of financial planning, basics of saving & investing, risk management, buying a home, marriage and family finance, retirement plan, tax planning, and financial education resources. You do not charge for this presentation.

The financial planning component consists of four steps:

- 1) Gathering the client's personal and financial data for the budget and planning;
- 2) Formulating a good budget by using a web-based budget formulating program of M;
- 3) Generating a financial plan by entering the budget and the client's data into N;
- 4) Monitoring and updating the plan.

You charge \$50 for the financial planning service. You stated that this fee is highly discounted from the market rate. M is a web based software package that provides a quick, one-page budget for your client and is available in the market. You pay \$10 for the software. The budgeting involves two to three one-hour meetings to develop a good budget for your client. You spend from 30 minutes to several hours with a client to formulate their financial plan. N is a financial planning software program that is available

in the market. You pay an annual fee of U for the software. The plan generated by N includes the following:

- Personal Information and Summary of Financial Goals
- Current Financial Goals Graph
- Net Worth
- Current Asset Distribution by Asset Class and Tax Category
- Current Portfolio Allocation
- Goal assignment Summary
- Asset Allocation Results: Risk Questionnaire, Target Portfolio, Results Comparison, Portfolio Detail, Changes Needed
- What if Worksheet - Scenarios
- What If Worksheet - Cash Used to Fund Goals
- What If Worksheet - Retirement Distribution Cash Flow Chart

You have four governing body members and will compensate your treasurer. Your financial data shows that your estimated contribution and donation income is expected to be around \$, \$, and \$ (respectively) for your first three years of operations. Income generated from service fees will be approximately \$ to \$ \$ per year as you expect that you will have 100 to 200 clients yearly at \$ per financial planning session.

We asked you to provide further details regarding how you formulate a good budget and generate a financial plan for the clients. You refused to provide further details regarding these activities. We also asked you to provide your future compensation plan for your governing members. You did not provide further details on that plan either.

Law

Section 501(c)(3) of the Code provides that corporations may be exempt from tax if they are organized and operated exclusively for charitable or educational purposes and no part of their net earnings inures to the benefit of any private shareholder or individual.

Section 501(q)(1)(D) of the Code provides that organizations which provide "credit counseling services" as a substantial purpose shall not be exempt from taxation under section 501(a) unless they are described in sections 501(c)(3) or 501(c)(4) and at all times organizations have a board of directors or other governing body--

- (i) which is controlled by persons who represent the broad interests of the public, such as public officials acting in their capacities as such, persons having special knowledge or expertise in credit or financial education, and community leaders,

(ii) not more than 20 percent of the voting power of which is vested in persons who are employed by the organization or who will benefit financially, directly or indirectly, from the organization's activities (other than through the receipt of reasonable directors' fees or the repayment of consumer debt to creditors other than the credit counseling organization or its affiliates), and

(iii) not more than 49 percent of the voting power of which is vested in persons who are employed by the organization or who will benefit financially, directly or indirectly, from the organization's activities (other than through the receipt of reasonable directors' fees).

Section 501(q)(4)(A) defines, for purposes of section 501(q), the term "credit counseling services" to mean (i) the providing of educational information to the general public on budgeting, personal finance, financial literacy, saving and spending practices, and the sound use of consumer credit; (ii) the assisting of individuals and families with financial problems by providing them with counseling; or (iii) a combination of the activities described above.

Section 1.501(c)(3)-1(a)(1) of the Income Tax Regulations ("regulations") provides that, in order to be exempt as an organization described in section 501(c)(3) of the Code, an organization must be both organized and operated exclusively for one or more of the purposes specified in such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt.

Section 1.501(c)(3)-1(c)(1) of the regulations provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities that accomplish one or more such exempt purposes specified in section 501(c)(3) of the Code. An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(d)(1)(ii) of the regulations assigns states it is necessary for an organization to establish that it is not organized or operated for the benefit of private interests, such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interests.

Section 1.501(c)(3)-1(d)(2) of the regulations provides that the term "charitable," is used in section 501(c)(3) in its generally accepted legal sense and includes the relief of the poor and distressed or of the underprivileged.

Section 1.501(c)(3)-1(d)(3)(i) of the regulations provides that the term "educational," as used in section 501(c)(3) of the Code, relates to:

- (a) The instruction or training of the individual for the purpose of improving or developing his capabilities; or

- (b) The instruction of the public on subjects useful to the individual and beneficial to the community.

In Rev. Rul. 69-441, 1969-2 C.B. 115, the Service found that a nonprofit organization formed to help reduce personal bankruptcy by informing the public on personal money management and aiding low-income individuals and families with financial problems was exempt under section 501(c)(3) of the Code. Its board of directors was comprised of representatives from religious organizations, civic groups, labor unions, business groups, and educational institutions.

Section 4.03 of Rev. Proc. 2011-9, provides that exempt status will be recognized in advance of operations if proposed operations can be described in sufficient detail to permit a conclusion that the organization will clearly meet the particular requirements of the section under which exemption is claimed. A mere restatement of purposes or a statement that proposed activities will be in furtherance of such purposes will not satisfy this requirement. The organization must fully describe the activities in which it expects to engage, including the standards, criteria, procedures or other means adopted or planned for carrying out the activities, the anticipated sources of receipts, and the nature of contemplated expenditures. Where the organization cannot demonstrate to the satisfaction of the Service that its proposed activities will be exempt, the Service will generally issue a proposed adverse determination letter or ruling.

In Better Business Bureau of Washington, D.C. v. U.S., 326 U.S. 279, 283, 66 S. Ct. 112, 90 L. Ed. 67 (1945), the Supreme Court held that the "presence of a single . . . [non-exempt] purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly . . . [exempt] purposes."

In American Institute for Economic Research v. United States, 302 F. 2d 934 (Ct. Cl. 1962), the Court considered an organization that provided analyses of securities and industries and of the economic climate in general. It sold subscriptions to various periodicals and services providing advice for purchases of individual securities. The court noted that education is a broad concept, and assumed *arguendo* that the organization had an educational purpose. However, the totality of the organization's activities, which included the sale of many publications as well as the sale of advice for a fee to individuals, was indicative of a business. Therefore, the court held that the organization had a significant non-exempt commercial purpose that was not incidental to the educational purpose, and was not entitled to be regarded as exempt.

For an organization claiming the benefits of section 501(c)(3), "exemption is a privilege, a matter of grace rather than right." Christian Echoes National Ministry, Inc. v. United States, 470 F.2d 849, 857 (10th Cir. 1972), *cert. denied*, 414 U.S. 864 (1973). The applicant for tax-exempt status under section 501(c)(3) has the burden of showing it "comes squarely within the terms of the law conferring the benefit sought." Nelson v. Commissioner, 30 T.C. 1151, 1154 (1958).

In B.S.W. Group, Inc. v. Commissioner, 70 T.C. 352 (1978), the Tax Court found that a corporation formed to provide consulting services did not satisfy the operational test under section 501(c)(3) of the Code because its activities constituted the conduct of a trade or business that is ordinarily carried on by commercial ventures organized for profit. Its primary purpose was not charitable, educational, or scientific, but rather commercial. In addition, the court found that the organization's financing did not resemble that of the typical section 501(c)(3) organizations. It had not solicited, nor had it received, voluntary contributions from the public. Its only source of income was fees from services, and those fees were set high enough to recoup all projected costs and to produce a profit. Moreover, it did not appear that the corporation ever planned to charge a fee less than "cost." Finally, the corporation did not limit its clientele to organizations that were section 501(c)(3) exempt organizations.

In Easter House v. U.S., 12 Cl. Ct. 476, 486 (1987), aff'd, 846 F. 2d 78 (Fed. Cir.) cert. denied, 488 U.S. 907, 109 S. Ct. 257, 102 L. Ed. 2d 246 (1988), the Claims Court found an organization that operated an adoption agency was not exempt under section 501(c)(3) of the Code because a substantial purpose of the agency was a non-exempt commercial purpose. The court concluded that the organization did not qualify for exemption under section 501(c)(3) because its primary activity was placing children for adoption in a manner indistinguishable from that of a commercial adoption agency. The court rejected the organization's argument that the adoption services merely complemented the health related services to unwed mothers and their children. Rather, the court found that the health-related services were merely incident to the organization's operation of an adoption service, which, in and of itself, did not serve an exempt purpose. The organization's sole source of support was the fees it charged adoptive parents, rather than contributions from the public. The court also found that the organization competed with for-profit adoption agencies, engaged in substantial advertising, and accumulated substantial profits. Accordingly, the court found that the "business purpose, and not the advancement of educational and charitable activities purpose of plaintiff's adoption service, is its primary goal" and held that the organization was not operated exclusively for purposes described in section 501(c)(3). Easter House, 12 Cl. Ct. at 485-486.

In Living Faith, Inc. v. Commissioner, 950 F.2d 365 (1991), the Court of Appeals upheld a Tax Court decision that an organization operating restaurants and health food stores in a manner consistent with the doctrines of the Seventh Day Adventist Church did not qualify for exemption under section 501(c)(3) of the Code because the organization was operated for a substantial non-exempt commercial purpose. The court found that the organization's activities were "presumptively commercial" because the organization was in competition with other restaurants, engaged in marketing, and generally operated in a manner similar to commercial businesses.

In Airlie Foundation v. Commissioner, 283 F. Supp. 2d 58 (D.D.C., 2003), the District Court relied on the "commerciality" doctrine in applying the operational test. Because of the commercial manner in which this organization conducted its activities, the court

found that it was operated for a non-exempt commercial purpose, rather than for a tax-exempt purpose. As the court stated: "Among the major factors courts have considered in assessing commerciality are competition with for profit commercial entities; extent and degree of below cost services provided; pricing policies; and reasonableness of financial reserves. Additional factors include, among other things, whether the organization uses commercial promotional methods (e.g., advertising) and the extent to which the organization receives charitable donations."

Application of Law

Based on the information provided in your application and supporting documentation, you are not operated for exempt purposes under section 501(c)(3) of the Code. You are organized for a substantial commercial purpose, operate in a commercial manner and for the benefit of private interests. Further details for this conclusion are set forth below.

Operational Test

To satisfy the operational test, an organization must establish that it is operated exclusively for one or more exempt purposes. See section 1.501(c)(3)-1(c)(1) of the regulations. An organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities that accomplish one or more of such exempt purposes as specified in section 501(c)(3) of the Code and Section 1.501(c)(3)-1(c)(1) of the regulations. Under the operational test, the purpose towards which an organization's activities are directed, and not the nature of the activities themselves, is ultimately dispositive of the organization's right to be classified as a section 501(c)(3) organization. See B.S.W. Group, Inc. v. Commissioner, *supra*. Your activities are not directed toward one or more exempt purposes. While you engage in presentations on personal finance that may, in part, further educational purposes, your activities primarily further the substantial non-exempt purpose of providing financial planning service. Thus, you have failed to establish that you are operated exclusively for one or more exempt purposes.

You Are Not Operated Exclusively for Charitable Purposes

Section 1.501(c)(3)-1(d)(2) of the regulations defines the term "charitable" as used in section 501(c)(3) of the Code as including the relief of the poor and distressed or of the underprivileged. You failed to show that your activity is charitable since you do not limit your services to a particular charitable class of people, such as low-income and elderly. Instead, your target clientele is middle and low-middle income households who earn around \$100,000 with substantial savings. Thus, you are unlike the organizations described in Rev. Rul. 69-441, above, which aided low-income individuals and families who have financial problems, and relieved the poor and distressed. Providing financial planning services for a fee to middle and low-middle income households does not provide relief to the poor and distressed within the meaning of section 1.501(c)(3)-1(d)(2) of the regulations or serve any other purpose recognized as charitable.

Your Activities Are Not Educational

Your operational focus is providing a good financial plan to the middle class for a fee. Your financial planning sessions with your clients do not have educational components since they consist of nothing more than formulating the budget provided by the client, and entering the client's financial information and the budget into a software program to generate a desired financial plan for your client. You have also failed to substantiate that you follow an educational methodology. Besides a 52 page Powerpoint presentation, which is a mere prelude for your selling of financial planning, you do not conduct any educational seminars, workshops, or forums. It is clear from your bylaws that your primary purpose is "assisting lower and middle-income families and individuals with the development of household financial, budgeting and savings plans" for a fee rather than financial education to the public as a whole. Accordingly, you are not an organization described in section 1.501(c)(3)-1(d)(3)(i) of the regulations.

You Have a Substantial Non-exempt Purpose

Section 1.501(c)(3)-1(c)(1) of the regulations provides that an organization operates exclusively for exempt purposes only if it engages primarily in activities that accomplish exempt purposes specified in section 501(c)(3) of the Code. Your organization engages in the substantial non-exempt activity of providing financial planning services to the public. You, therefore, do not operate exclusively for exempt purposes.

Your Form 1023 application and responses demonstrate that you operate for the substantial non-exempt purpose of operating a financial service business. See, Better Business Bureau of Washington D.C., Inc. v. United States, 326 U.S. 279 (1945), in which the Supreme Court held that the presence of a single non-exempt purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly exempt purposes.

Your financial planning service is similar to that of a commercial financial planning business. You initially offer a free presentation to your potential clients, which stresses the need for financial planning. Following the presentation, you offer your financial planning service; therefore the presentation serves as an overture for your financial service for a fee, which is a common practice in selling financial instruments or planning services. The only difference from the commercial planning service is that you offer your services at a substantially discounted price. However, offering a discounted price does not make you charitable, rather it puts you in a better position to compete with commercial financial services because you will have a low-price advantage over your competitors. Therefore, your business directly competes with commercial financial planning service entities. The court found that an organization that conducts a commercial business and competes with commercial companies does not qualify for exemption under 501(c)(3) in Easter House v. U.S. and Living Faith, Inc. v. Commissioner, regardless of the organizations' doctrines.

In B.S.W. Group, Inc. v. Commissioner and Airlie Foundation v. Commissioner, above, the courts concluded that running a consulting service and a conference center are not an exempt activity for the reason of commerciality, which is applicable to your financial planning service. The courts pointed out the dependency of the income from the operation and competition with commercial entities for the characteristics of commerciality. You possess such commercial characteristics. The court in American Institute for Economic Research v. United States, above applied an even more stringent interpretation. The court held that an educational organization was not entitled to exemption because it conducted the sale of many publications as well as the sale of advice to individuals. You are similar to this organization in terms of selling financial planning services to the public.

Private Benefits/Inurement

Your financial planning services serve the private benefit of your clients more than incidentally, resulting in personal gain to them. When you provide financial services to your clients at a fee of \$50, your clients no longer have to pay a higher fair market fee to commercial financial planning service firms. Therefore, your discounted financial service results in impermissible private benefit to your clients rather than a public interest in contravention of section 1.501(c)(3)-1(c)(1) and section 1.501(c)(3)-1(d)(1)(ii) of the regulations by providing them discounted financial services. In addition, you have failed to show that your organizational structure and manner of operation will not result in inurement to your governing members in the form of compensation in accordance with section 1.501(c)(3)-1(d)(1)(ii) of the regulations because you did not provide your financial data in sufficient detail to permit a conclusion that you will not compensate your governing members excessively. See section 4.03 of Rev. Proc. 2011-9.

Section 501(q) of the Code

An organization that provides educational information on financial topics or financial counseling to homeowners who are at risk of foreclosure is providing "credit counseling services" within the meaning of section 501(q)(4)(A) of the Code. Thus, even if you engage in substantial non-financial counseling activities to be exempt from taxation you must, in addition to complying with the requirements of section 501(c)(3), comply with the provisions of section 501(q).

You have four governing members and at least one of them will be compensated. Therefore, your governing body does not comply with section 501(q)(1)(D)(ii) that requires that at all times the organization must have a board of directors or other governing body not more than 20 percent of the voting power of which is vested in persons who are employed by the organization or who will benefit financially, directly or indirectly, from the organization's activities, because one out of four board members directly benefits from your organization's activities. Furthermore, you failed to show that you will meet the requirement of section 501(q)(1)(D)(ii) at all times as you chose not to provide further response on this

matter. See Christian Echoes National Ministry, Inc. v. United States, above and Nelson v. Commissioner, above. The courts concluded that the burden of proof is on the applicant organization to demonstrate that it has met the operational test as specified under section 501(c)(3) of the Code.

Conclusion

Based on the facts and information provided, you are not organized or operated exclusively for exempt purposes as required the regulations. You are operated for commercial purposes in contravention of the regulations and for the benefit of private interests. Any public purposes for which you may operate are only incidental to this primary non-exempt purpose. Therefore, you are not described in section 501(c)(3) of the Code.

You have the right to file a protest if you believe this determination is incorrect. To protest, you must submit a statement of your views and fully explain your reasoning. You must submit the statement, signed by one of your officers, within 30 days from the date of this letter. We will consider your statement and decide if the information affects our determination. If your statement does not provide a basis to reconsider our determination, we will forward your case to our Appeals Office. You can find more information about the role of the Appeals Office in Publication 892, *Exempt Organization Appeal Procedures for Unagreed Issues*.

Types of information that should be included in your appeal can be found on page 2 of Publication 892, under the heading "Regional Office Appeal". These items include:

1. The organization's name, address, and employer identification number;
2. A statement that the organization wants to appeal the determination;
3. The date and symbols on the determination letter;
4. A statement of facts supporting the organization's position in any contested factual issue;
5. A statement outlining the law or other authority the organization is relying on; and
6. A statement as to whether a hearing is desired.

The statement of facts (item 4) must be declared true under penalties of perjury. This may be done by adding to the appeal the following signed declaration:

"Under penalties of perjury, I declare that I have examined the statement of facts presented in this appeal and in any accompanying schedules and statements and, to the best of my knowledge and belief, they are true, correct, and complete."

Your appeal will be considered incomplete without this statement.

If an organization's representative submits the appeal, a substitute declaration must be included stating that the representative prepared the appeal and accompanying documents; and whether the representative knows personally that the statements of facts contained in the appeal and accompanying documents are true and correct.

An attorney, certified public accountant, or an individual enrolled to practice before the Internal Revenue Service may represent you during the appeal process. If you want representation during the appeal process, you must file a proper power of attorney, Form 2848, *Power of Attorney and Declaration of Representative*, if you have not already done so. You can find more information about representation in Publication 947, *Practice Before the IRS and Power of Attorney*. All forms and publications mentioned in this letter can be found at www.irs.gov, Forms and Publications.

If you do not file a protest within 30 days, you will not be able to file a suit for declaratory judgment in court because the Internal Revenue Service (IRS) will consider the failure to appeal as a failure to exhaust available administrative remedies. Code section 7428(b)(2) provides, in part, that a declaratory judgment or decree shall not be issued in any proceeding unless the Tax Court, the United States Court of Federal Claims, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted all of the administrative remedies available to it within the IRS.

If you do not intend to protest this determination, you do not need to take any further action. If we do not hear from you within 30 days, we will issue a final adverse determination letter. That letter will provide information about filing tax returns and other matters.

Please send your protest statement, Form 2848, and any supporting documents to the applicable address:

Mail to:

Internal Revenue Service
EO Determinations Quality Assurance
Room 7-008
P.O. Box 2508
Cincinnati, OH 45201

Deliver to:

Internal Revenue Service
EO Determinations Quality Assurance
550 Main Street, Room 7-008
Cincinnati, OH 45202

You may fax your statement using the fax number shown in the heading of this letter. If you fax your statement, please call the person identified in the heading of this letter to confirm that he or she received your fax.

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

Lois Lerner
Director, Exempt Organizations

Enclosure, Publication 892